IN THE

Supreme Court of the United States

OCTOBER TERM, 1979

NO. 79-793

HOUSTON LIGHTING AND POWER COMPANY,
Petitioner
and
ARIZONA ELECTRIC POWER COOPERATIVE, INC.,
Petitioner
v.
INTERSTATE COMMERCE COMMISSION, et al.,
Respondents

BRIEF OF THE CITY OF HOUSTON, TEXAS AMICUS CURIAE IN SUPPORT OF JOINT PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE DISTRICT OF COLUMBIA CIRCUIT

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The City of Houston, Texas, respectfully files this brief as *amicus curiae* in support of the Joint Petition of Houston Lighting and Power Company ("HL&P") and Arizona Electric Power Cooperative, Inc. ("Arizona") for a Writ of Certiorari to the United States Court of Appeals for the District of Columbia Circuit.

INTEREST OF THE CITY OF HOUSTON[1]

The City of Houston has a vital interest in the outcome of this case as a regulatory authority setting the rates Petitioner HL&P may charge for electricity sold within the City of Houston and as the lawfully constituted guardian of the public interest.

The City of Houston bears the brunt of the unjustifiably high coal freight rate sanctioned by the ICC and the lower court in this proceeding, because such costs are passed through by HL&P to its customers, most of whom live in the Houston metropolitan area.[2]

The City of Houston is adversely affected by said unreasonably high coal rates in several ways. First, City of Houston residents, particularly those with lower incomes, suffer undue hardship by needless increases in the cost of this basic necessity. Second, City of Houston residents are subsidizing residents in other areas of the country because the coal freight rate charged to HL&P is disproportionately higher than the rates charged on coal moving to other cities. Third, the disproportionately high cost of shipping coal to Houston unfairly and improperly dilutes the competitive advantage enjoyed by Houston businesses in the nation's marketplaces. These adverse effects will continue to worsen as HL&P increases the proportion of its electric power generated from coal.

1. The City of Houston was incorporated on January 28, 1839 (Laws of the Republic of Texas, 3d Congress, 1st Sess.), and is now a home rule city under Art. XI, § 5 of the Texas Constitution. As such it is empowered to "plead and be impleaded in all courts, and to act in perpetual succession as a body politic." (Vernon's Ann. Civ. St., Art. 1175, § 3).

2. 1978 Annual Report of Houston Industries Incorporated (hereinafter, "1978 Annual Report"), page 5.

Therefore, the City of Houston has a most vital interest in overturning the action of the ICC and the court below which errs to the detriment of the public interest of residents in the Houston area.

REASONS FOR GRANTING THE WRIT

1. The Decisions Below Aggravate the Upward Inflationary Spiral.

For many years, Houston has relied on the southwest's cheap and abundant natural gas and petroleum reserves to meet its expanding energy requirements. As recently as 1978, natural gas still constituted 98% of the fuel used by HL&P's generating facilities.[3] Beginning in the early 1970's, however, domestic supply shortages and the actions of the Organization of Petroleum Exporting Countries ("OPEC") began rapidly escalating the cost of natural gas and petroleum.

These fuel cost increases have necessitated substantial and consistent increases in HL&P's electric rates. Between 1974 and 1977, for example, the average rate per kilowatt-hour paid by HL&P's residential customers increased by 49%.[4] By contrast, during the same period, the average rate for residential customers in the nation as a whole increased by only 34%.[5] Since 1977,

3. 1978 Annual Report, p. 10.

4. *Id.*, p. 22.

5. Edison Electric Institute, *Statistical Yearbook of the Electric Utility Industry for 1977*, (hereinafter, "1977 Yearbook"), p. 53 (table 45S).

HL&P's fuel costs have continued, this upward spiral. For instance, the company's average fuel cost per "BTU"[6] climbed 19.6% between 1977 and 1978[7]. By the end of 1978, fuel costs had become more than 52% of its revenues.[8]

The escalating cost and scarcity of HL&P's traditional fuels, coupled with the nation's stated energy policy to develop increased reliance on other, more abundant domestic fuels, led HL&P to seek alternative fuel sources. The Company's long term plan includes a gradual shift from natural gas to coal and nuclear power as its predominant fuel sources.[9]

Coal is one of this nation's most important alternatives to the inflationary spiral triggered by OPEC price increases. HL&P's coal conversion program was designed to provide some measure of relief to consumers from ever-increasing electric rates. Although a coal-fired generating station costs five to ten times as much to build as does a gas-fired generating plant of equal capacity,[10] HL&P anticipated achieving long run savings through conversion to coal. Because coal is ordinarily much

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6. A "BTU," or "British Thermal Unit," is the amount of energy required to raise the temperature of one pound of water one degree fahrenheit.

7. 1978 Annual Report, p. 22.

8. *Id.*, p. 4.

9. *Id.*, p. 10.

10. Statement of George W. Oprea, Executive Vice President of Houston Lighting and Power Company, April 16, 1979, before the Subcommittee on Oversight and Investigations of the House Committee on Interstate and Foreign Commerce, p. 2. (Hearings not yet printed.)

cheaper per BTU than gas is,[11] increased coal usage should have reduced HL&P's fuel costs over the life of the plant enough to compensate for the higher initial capital cost.

However, HL&P's anticipated leveling off of electricity rate increases dissipated in the wake of the ICC and the Trial Court. Houston residents already must bear the inflationary capital costs of HL&P's $500 million coal-fired generating units at Smithers Lake, Texas, and should be able to anticipate compensatory fuel savings. However, if the decisions below are allowed to stand, they will not receive the appropriate compensating benefit of reduced fuel costs.

The decisions below depart from traditional ratemaking principles in that they permit the railroads to fix their coal freight rate with reference to the higher cost of oil and natural gas and thereby soak up most or all of the price differential between coal and gas. Such a policy allows the ever increasing OPEC prices to affect coal transport and to continue the inflationary spiral.

HL&P established before the ICC that the maximum reasonable rate on its coal traffic under traditional ratemaking principles, would be $10.44 per ton.[12] The $5.16 per ton difference between that rate and the $15.60 rate approved by the ICC requires HL&P's ratepayers to con-

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11. 1977 Yearbook, p. 51.

12. See pages 200-206 of the Opening Statement of Fact and Argument filed by HL&P on June 7, 1977 in *Docket No. 36579, Houston Lighting and Power Company v. Burlington Northern Inc., et al.* (This was the "complaint case" which was subsequently mooted by the "capital incentive" case at issue here.) See also The Joint Appendix in No. 77-2070 in the court below, Vol. III, page 602.

tribute an additional $25.8 million per year to subsidize the railroads' non-coal traffic.

The rate authorized by the ICC will cost HL&P customers approximately $40 million more annually than the rate initially quoted by the railroads. In addition, as HL&P approaches 100% conversion to coal, it will need approximately twenty times as much coal as it now uses.[13] In that event, a conservative estimate is that the railroads' extra profits, exacted from HL&P's ratepayers, could exceed half a billion dollars per year. This estimate is even more understated in that it does not take into account future increases in HL&P's fuel requirements as sales continue to grow. The spread between (a) reasonable (cost-based) rail rates, and (b) unreasonable (demand-based) rail rates, which soak up the entire coal/gas price differential, will increase significantly as gas and oil prices continue to rise faster than coal prices.

Regulation operates as a substitute for competition where a monopoly exists in order to prevent price abuse. Instead, the ICC has, in essence, itself based rates on what the market will bear. The ICC discarded comparable rates with similar cost characteristics on the basis that they were "depressed" by competition and chose instead to use a comparable rate standard based on an inflated value of service.

The primary cause of this nation's rampant inflation is the escalating cost of energy, resulting from OPEC's repeated price increases on petroleum, and from the recurring supply shortages of natural gas. The most

13. Hearings, *supra*, note 10.

important alternative available to free this country from its dependance on OPEC triggered inflation is to increase the use of America's abundant domestic coal reserves, which have not been rising in price as quickly as oil and gas. Conversion to coal generated plants is a logical step toward controlling energy cost increases, and thereby abating inflation. The decisions below have frustrated HL&P's efforts to achieve that goal.

Because of the enormous public importance of controlling needless inflation now, the City of Houston respectfully urges the Supreme Court to grant certiorari to review and correct the decisions below.

2. The Disproportionately High Freight Rate on HL&P's Coal Is Unduly Discriminatory to City of Houston Residents.

The freight rate set by the ICC for HL&P coal is substantially in excess of any rate considered reasonable under traditional ratemaking standards. The HL&P coal rate is also substantially in excess of the ICC authorized coal freight rates to other areas of the country.[14] Said rates are unduly prejudicial to the Houston area and unduly preferential to other regions of the country. As such, they are a violation of the fundamental Constitutional principal prohibiting discrimination between communities. "[T]he Commission [ICC], exercising a delegated regulatory authority which does not have the freedom of ownership, operates in a field *limited by constitutional rights.*" *Atchison, Topeka & Santa Fe Ry. Co. v. United States*, 284 U.S. 248, 252 (1932) (Emphasis added)

14. Joint Appendix in No. 77-2070, Vol. II, pages 60-61, 171-72.

Such discrimination between areas of the country is specifically condemned by the Interstate Commerce Act. This Court recognized in *New York v. United States*, 331 U.S. 284 (1947) that discrimination is the principal evil at which the Interstate Commerce Act was aimed. In furtherance of that central purpose the Act was amended in 1940 to provide:

> *It shall be unlawful for any common carrier . . . to make, give, or cause any undue or unreasonable preference* or advantage *to any particular* person, company, firm, corporation, association, *locality,* port, port district, gateway, transit point, *region, district, territory,* or any particular description of traffic, in any respect whatsoever; *or to subject any particular* person, . . ., *locality,* . . ., *region, district, territory,* . . ., *to any undue or unreasonable prejudice or disadvantage* in any respect whatsoever . . . . (Emphasis added)[15]

This Court, noting that the references to preference or prejudice to a "region, district, [or] territory" were added in 1940, explained:

> Congress, by adding those words, made plain the duty of the Commission in determining whether discriminatory practices exist to consider the interests of regions, districts, and territories, and to eliminate territorial rate differences which are not justified by differences in territorial conditions. *New York v. United States, supra,* 331 U.S. at 300.

15. Section 3(1) was recodified without substantive change as 49 U.S.C. § 10741(b) by P.L. 95-473, 92 Stat. 1337. As recodified it provides that "A common carrier . . . may not subject a person, *place,* port, or type of traffic to unreasonable discrimination." (emphasis added)

In the case before this Court today, HL&P has demonstrated that, at the time of the hearing before the ICC, the $15.60 coal freight established for HL&P is substantially higher, on a ton-mile basis, than the rates the railroads were then charging on unit coal trains serving other communities.[16]

The Company also demonstrated that the disparities could not be supported by differences in relevant transportation conditions. Far from supporting such disparities, the evidence presented before the ICC supports lower rates for HL&P than for other coal receivers.[17] Yet, both the ICC and the lower Court dismissed HL&P's claims of discrimination on the ground that HL&P had not shown that it was competitively injured by the rate disparities. In so doing they applied the wrong test, contrary to constitutional restrictions and the legislative mandate expressed by this Court in *New York v. United States, supra.*

HL&P did not and could not show competitive harm to itself. As a regulated public utility, it is not in competition with utilities serving other areas. The relevant competitive harm from discriminatory coal freight rates to HL&P is the harm to HL&P's customers, and to the region it serves (in particular, to the City of Houston). The unreasonable coal freight rate disparities artifically inflate the cost of living and the cost of doing business in Houston as compared to cities with preferential coal freight rates. Such rates dilute Houston's natural economic advantage to attract new industries and dilute the competitive strength of existing Houston businesses.

16. Joint Appendix, *supra,* note 15, *loc. cit.*

17. *Id.*

This Court recognized that discriminatory rates can have the effect of impeding industry and arresting area development in the *New York* case:

> We assume that a case of unlawful discrimination against shippers by reason of their geographic location would be an unlawful discrimination against the regions where the shipments originate. But an unlawful discrimination against regions or territories is not dependent on such a showing. As we stated in *Georgia v. Pennsylvania R. Co.,* 324 U.S. 439, 450, 65 S. Ct. 716, 723, 89 L. Ed. 1051, 'Discriminatory rates are but one form of trade barriers. Their effect is not only to impede established industries but to prevent the establishment of new ones, to arrest the development of a State or region, to make it difficult for an agricultural economy to evolve into an industrial one . . . .'
>
> If a showing of discrimination against a territory or region were dependent on a showing of actual discrimination against shippers located in these sections, the case could never be made out where discriminatory rates had proved to be such effective trade barriers as to prevent the establishment of industries in those outlying regions. If that were the test, then the 1940 amendment to § 3(1) would not have achieved its purpose. We cannot attribute such futility to the effort made by Congress to make regions, districts and territories, as well as shippers, the beneficiaries of its anti-discrimination policy expressed in § 3(1). New York v. United States, *supra,* 331 U.S. at 308.

Moreover, while some harm to the disfavored region must still be shown in order for the rate disparity to violate § 3(1), *New York* recognized that

> The causal connection between rate discrimination and territorial injury is not always susceptible of conclusive proof. The extent of that causal relation cannot in any case be shown with mathematical exactness. It is a matter of inference from relevant data. . . .
>
> 'Nearness to markets and ability to ship to markets, on a basis fairly and reasonably related to the rates of competitors, are . . . potent factors in the location of a manufacturing plant. In fact, rate relations are more important to the manufacturer and shipper than the levels of the rates.' 262 I.C.C. 619, 620. *New York v. United States, supra,* 331 U.S. at 310.

In *New York,* the finding of prejudice was made difficult by the fact that very little traffic actually moved at the class rates in question. 331 U.S. at 306-7. No such complication exists here; HL&P demonstrated that the disparity between its rate and those available to other receivers, could cost it (and, therefore, its ratepayers) almost $18 million per year.[18] No clearer case of actual and direct prejudice to the Houston area could be presented.

By focusing solely on injury to HL&P, both the agency and the court below ignored the Court's direction in *New York.* Such interpretation effectively reads the prohibition against inter-regional preferences or prejudices right out of the Interstate Commerce Act. Because of the ominous implications such a narrow reading of § 3(1) holds for our nation's carefully-balanced common carrier transportation network, the City of Houston re-

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18. Joint Appendix, *supra* note 15, at page 60.

spectfully urges the Supreme Court to grant certiorari to review and correct the decisions below.

CONCLUSION

The City of Houston recognizes that the railroads must be permitted to charge rates on all their traffic, including coal, that will cover their costs and afford them reasonable profits. However, the City of Houston cannot stand idly by while the ICC sanctions rates on HL&P coal traffic that are far higher than are necessary or reasonable for that purpose, in order to cross-subsidize other regions and other traffic. As the Eighth Circuit noted in *Burlington Northern Inc. v. United States*, 555 F.2d 637,

> . . . the rates for a unit train movement [of coal should be] . . . structured to 'stand on their own wheels'. . . . Unless they are so structured, the consumers of one community may end up subsidizing the consumers of another . . . . The movement of coal in the years ahead will be too important to permit this to happen . . . .

The rate approved on HL&P's coal traffic violates this fundamental principle prohibiting cross-subsidies between communities.

The freight rates established by the ICC for HL&P coal unfairly penalize the residents of Houston by frustrating their efforts to control energy-based inflation. Such rates also unfairly prejudice the ability of Houston and its industries to compete in the national marketplace and have the effect of arresting area development.

For all of these reasons, the City of Houston respectfully urges the Supreme Court to grant HL&P's petition for certiorari to review and correct the decisions below.

Respectfully submitted,

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